SAN LUIS OBISPO COUNTY COMMUNITY FOUNDATION

Turning Passion into Action

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Charitable Giving: Donor and Charity Concerns

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Disclaimer: This presentation does not provide legal advice. Readers are encouraged to consult their professional advisors.

Donor Concerns

1. How do I know a nonprofit is legitimate?*

- Verify organization on GuideStar [verifies technical compliance with IRS].
    - California Attorney General's Office has outsourced its verification to GuideStar.
    - GuideStar is an on-line database of nonprofit organizations [www.guidestar.org].
- Double-check the charity's name; similar names can be confusing. United Way is different than United Crusade or Another Way.
- Call the organization:
    - Ask how the organization carries out its mission, and what has it accomplished lately.
    - Ask what percentage of donation dollars go to the actual charitable purpose [501(c)(3); there are 28 classifications of 501(c) organizations].
    - Ask for web site address.
    - Ask to review the organization's Form 990.

*Due diligence must be commensurate with amount of gift.

2. How can I make sure my gift is being used wisely?

<u>Transparency</u>: Deliberately revealing actions. As public corporations, nonprofits build trust by being public, understanding that there are laws regarding specific employment conditions and health-related topics. Nonprofits are required to provide a copy of their most recent audited financial statements upon request (they can charge a fee for photocopying and mailing). A list of the members of the Board of Directors is public and should be readily available.

Be careful of comparisons!

- National Center for Charitable Statistics found that you get what you pay for [www.coststudy.org]. Nonprofits that limit spending on administration and fundraising are less effective than comparable organizations. Furthermore, pressure to report low administration ("overhead") costs leads to misrepresentation of the true cost of delivering a program or service.
- Ellison Research (February 2008) found that Americans feel that it is reasonable for a nonprofit to spend 22.4% on administration ("overhead"). [www.ellisonresearch.com/releases/0208_ERWhitePaper.pdf]
- American Institute of Philanthropy holds that 40% or more for administration ("overhead") is too much. [www.charitywatch.org/tips.html]

"One doesn't fall in love with someone based on their 1040.
So why does someone fall in love with a charity based on its 990?"
Doug White, 2007.

3. How much is too much to give?

A. Donor Perspective:

- Americans gave 2.3% of income to charity in 2006, or $3,692 on average.
- Californians gave $3,834 on average.
- Nonprofit planners peg a major gift as 5% of prospect's net assets.

B. Deduction Limits:

- A donor may give and deduct up to 50% of his or her AGI in one year (assuming no net operating loss). If the donor gives more than the 50% limit, the excess is carried forward and may be deducted over the next five years.
- A donor may deduct the full value of a long-term appreciated asset (held at least for one year and one day) but the charitable gift limit is 30% of AGI.
- A donor may deduct cost basis for a short-term appreciated asset (held less that one year and one day) and the charitable gift limit is 50% of AGI.

C. "Tipping" is more than 10%:

Question: XYZ charity operates out of the founder's home, and receives on average $4,000 in donations per year. Will a one-time $10,000 gift "tip" the organization?

- Public Support Test
    - "Public" charities must prove they are publically supported
        - Mechanical Test: 1/3 public support
        - Facts & Circumstances Test:
            - Less than 33.4% but more than 10%
            - Various factors showing spirit of public support
        - Both tests are based on four years of data
        - "Public Support" can't include more than 2% (of total support) from any one donor
    - A large gift to a small charity, especially one that is young, may "tip" the organization into a private foundation.
        - Gift deduction limits are reduced for private foundations

A good summary of the Public Support Test is at
http://www.sharinglaw.net/npo/PublicSupportTest.htm

4. What documentation does the donor need to provide?

A. Gifts of Cash: Donor must maintain a canceled check or receipt evidencing each contribution (including name of charity, date, and amount).
B. Gifts of Property: For gifts of property to which the appraisal rules do not apply (see below), the donor must maintain a receipt from the charity showing the name of the charity, the date and location of the gift, and a description (but not value) of the property. If it is impractical to obtain a receipt, the donor must retain "reliable written records" containing the above information plus information regarding the value of the contribution. Note that donations of clothing and "household items" are not allowed unless they are in at least "good used" condition. If the deduction for a gift of property exceeds $500, the donor must maintain a written record including the above information plus the manner and date of acquisition and cost basis…and complete IRS Form 8283.

C. Appraisal Rules

i. Need for an appraisal

An appraisal is required of gifts of property where the deduction claimed exceeds $5,000. No deduction is allowed unless the donor: obtains a qualified appraisal from a qualified appraiser; attaches an appraisal summary to the tax return on which the deduction is first claimed (i.e., Form 8283); and maintains the records described above for gifts of property.

No qualified appraisal, and only a partial appraisal summary, is required for gifts of publicly traded securities or non-publicly traded stock not exceeding $10,000 in value.

If the claimed deduction is over $500,000, the donor must attach a copy of the appraisal to his/her return.

ii. Timing

A qualified appraisal must be signed no earlier than 60 days before the date of gift, or later than the due date of the taxpayer's tax return on which he/she first claims the deduction. It must have an effective date no earlier than 60 days before the date of the gift, or later than the date of gift.

iii. Information

Regulation Section 1.170A-13(c)(3) sets forth a long list of information that must be included in the appraisal, including:

1. Description of the property.
2. Date of gift and effective date of the appraisal.
3. Terms of any agreement relating to charity's use or sale of property.
4. Statement that appraisal is for tax purposes.
5. Value and valuation method.
6. Qualifications of the appraiser.

An appraisal must be conducted "in accordance with generally accepted appraisal standards", be made by a "qualified appraiser", and not involve an appraisal fee that is based on the appraised value of the property.

It is helpful if the appraisal contains a declaration by the appraiser acknowledging that he/she may be subject to penalties for valuation misstatements.

If the donor contributes a partial interest in property, the appraisal must be of the partial interest.

iv. Qualified appraiser

A "qualified appraiser" is now defined as someone who:

1. Regularly performs appraisals for compensation;
2. Has verifiable education and experience in valuing the type of property being valued (meaning he/she has either earned an appraisal designation from a recognized professional appraiser association or has met minimum education and experience levels);
3. Understands he/she may be subject to penalties for aiding and abetting the understatement of tax;
4. Is not the donor, donee, or any party to the transaction in which the donor acquired the property;
5. Is not any person employed by or related to one of the above parties;
6. Is not someone primarily used by one of the above parties who does not perform a majority of his or her appraisals for other persons; and
7. Has not been prohibited from practicing before the IRS at any time during the three-year period ending on the date of the appraisal.

Appraisal Rules are not optional.

Charity (Recipient) Concerns

1. When is a gift a gift?

Regulation Section 1.170A-1(b) says a contribution is made at the time delivery of the gift asset is effected.

> "Charity begins where certainty of beneficiary ends."
> Erik Dryburgh, 2008

There are three components of a gift:

- Intent
- Transfer of Asset
- Acceptance

Question: Darcie Donor responds to the year-end mailing by sending a $250 check to XYZ charity. The postmark date is December 24. The check arrives at XYZ on December 31, and is processed on January 2. When did Donor make the gift?

A. Donation by Check
The unconditional delivery of a check that clears in "due course" is deemed to be given on date of delivery.

B. Donation by Credit Card
A contribution made by credit card is deductible in the year in which the charge is made, regardless of when paid.

Question: On December 29, Phil Anthropist instructs his stock broker to transfer 100 shares of IBM to XYZ Charity. The stock hits the charity's account on January 2. When did the gift occur?

C. Donation of Stock
The delivery of a properly endorsed certificate (or stock certificate and signed stock power) to charity (or its agent) is deemed given on the date of delivery.

Alternative: the gift is complete when ownership of the stock is transferred on the corporation's books and records. In the case of stock held in street name, the gift is complete when ownership of the stock is transferred out of the donor's account.

Question: Jenny Bigshot is a director at Endrun Corp. and donates 1,000 shares of Endrun Corp. common stock to XYZ charity. Bigshot calls XYZ's CEO and comments, "I'm not going to sell any of my stock for two weeks." What gift has Bigshot made?

D. Mailbox Rule
A check (or stock) that is mailed to the charity, and received in due course, is deemed to be given on date of mailing (date of stamp cancellation). In the case of package delivery service, such as FedEx, FedEx is the donor's agent because the donor can cancel package delivery up until the delivery is made. In this case, the date of delivery is the date that the package is received by the charity.

E. Real Property and Tangible Personal Property
Delivery of tangible personal property usually requires an actual transfer of possession. In some cases, constructive delivery can be shown. Gifts of real estate require the delivery of a formally executed and acknowledged (notarized) deed; title does not have to be recorded to have a completed gift.

Key question for real property: who owns the property?

Question: XYZ charity sells $100 raffle tickets with the winner receiving a Mini Cooper car, valued at $20,000. Goody Twoshoes owns the winning ticket and asks that instead of the car the charity send a check for $15,000 cash and a receipt for a $5,000 donation to the charity, and urges the charity to sell the car for whatever amount it wants. What gift has Twoshoes made?

2. What documentation is required?

Charity must provide a contemporaneous written acknowledgment for all donations of $250 or more. However, it is the donor's obligation to obtain the receipt. The receipt must include:

1. The amount of cash and/or description (but not value) of any property given.
2. Whether the charity provided goods or services in consideration for the gift.
3. A description and good faith estimate of the value of any goods or services provided (except for intangible religious benefits, which must be noted).
4. Date of receipt of the donation.
5. Name of the donor(s).

For donations of vehicles, the charity must issue a receipt containing: the name and ID# of the donor, the vehicle's VIN, the gross sales proceeds received upon the sale of the vehicle and a statement that the deduction is limited to sales proceeds (unless the charity puts the vehicle to a significant intervening use or materially improves it). The receipt is due 30 days after sale.

Question: Popeye T. Sailorman donates a boat to XYZ charity, a Shandon-based organization that promotes sustainable agriculture. What gift has been made?

In addition to the usual information, a charity receiving a gift to a Donor Advised Fund must, in its receipt, must state that it has "exclusive legal control over the assets contributed".

The Tattle-Tale Rule: A charity that sells, exchanges, or otherwise disposes of "charitable contribution property" within 3 years of receipt must file a Form 8282, disclosing the disposition and amount received. Charitable contribution property means property with respect to which the charity signed a Form 8283 (i.e., property for which an income tax deduction was claimed in excess of $5,000).

If a charity receives tangible personal property, puts it to a related use, and then sells it within 3 years, an officer must sign a written statement under penalty of perjury certifying that the charity's use was related to its exempt purpose and attach it to the Form 8282.

Question: Paula Picasso donates the watercolor landscape she painted. What is the gift value?

Donors of self-created original works are entitled to deduct the <u>cost</u> of producing the original works. However, if the donor is not the creator, then the donor is entitled to deduct the fair market value of the item.

3. Can a gift be rejected?

Yes. If a gift comes with strings, the charity accepts the gifts AND the strings.

Sometimes the strings will disqualify the gift:

- Donor retains the right to redirect the purpose of the gift (this is different from a Donor Advised Fund)
- Donor retains the right to take back the gift if conditions are not met

- Donor retains the right to develop land or market a patent
- Appraisal rules are not followed

Question: Ritchey Rich donates money to start a new program at XYZ charity but asks that he be allowed to approve of the program director. What gift has been made?

Sometimes the charity doesn't want the reality of the gift:

- Gift requires creation of new program or service
- Too steep matching requirement
- Requirement to permanently restrict the gift
- Gift funds only a portion of program or service
- Hard to value or market private company shares
- Partial interest in asset
- Requirement to hold asset for period of time
- Naming/recognition requirements
    - University of Missouri-Columbia: "Kenneth Lay Chair"
    - Seton Hall University: Koslowski Hall
    - Michael Milken School

Resources used in preparing this presentation:

Council on Foundations. www.cof.org.

Dryburgh, Erik. "Donor Restrictions: What Will They Think of Next?" Conference of League of California Community Foundations, San Francisco, September 8, 2008.

Dryburgh, Erik. "What Do You Have to Do to Complete the Gift?" Conference of League of California Community Foundations, San Francisco, September 8, 2008.

Gift Law Pro from Crescendo Interactive, Inc.

Libengood, Dave. "Charitable Giving Case Studies: The Practical and the Complex." Joint meeting of the the Estate Planning Council of San Luis Obispo County and the Central Coast Planned Giving Council, July 23, 2008.

White, Doug. "Charity on Trial." Meeting of Central Coast Planned Giving Council, October 9, 2007.

Comparison of Donor Advised Fund at the Community Foundation
to a Private or Family Foundation

Donor Advised Fund	*Private or Family Foundation*
1. No initial tax filings	1. Must file documents with IRS requesting status of Foundation
2. No incorporation documents required	2. Must establish corporation
3. Cash Gifts Deductible at 50% AGI	3. Cash Gifts Deductible at 30% AGI
4. Appreciated Assets Deductible at 30% AGI	4. Appreciated Assets Deductible at 20% AGI
5. Real Estate contributed during life deductible at Fair Market Value	5. Real Estate contributed during life deductible at basis
6. No Excise Taxes	6. Excise Taxes of 2% of Net Investment Income
7. No annual pay-out requirement	7. Pay-out required: 5% of assets annually
8. Low management fee pays accounting, legal & tax services	8. Costly accounting, legal & tax services
9. Professional staff Professional investment management	9. Most Private Foundations are too small to afford staff and liability insurance.
10. Anonymity if desired	10. 990 PF available to all via internet
11. Regular reports with history of gifts and grants	
12. Committed to help donors achieve charitable goals	